

ICPS newsletter®

Fiscal transparency is key to efficient government

On one hand, decentralization in Central European and FSU countries has placed more responsibility on local governments; on the other, it has given them more money to work with. Taxpayers want to be sure that this money is spent properly. Fiscal transparency lets voters follow their money through the labyrinthine processes of budgeting and spending. The latest issue of "Gosudarstvennoye upravlenie v perekhodnykh ekonomikakh," the Russian-language version of the Local Governance Brief translated and distributed by the International Centre for Policy Studies, emphasizes the importance of fiscal transparency and proposes ways to improve it

Promoting the honest, efficient management of public money in local governments is a condition of democracy. Inefficient or corrupt local government can hinder development and erode faith in democracy. Fiscal transparency allows taxpayers to act like customers, demanding the most value for their money. Through fiscal transparency, local stakeholders can help make sure that public funds are used well.

Local budget watch

The work of maintaining fiscal transparency at the municipal level is often referred to as "local budget watch." The most traditional focus of budget monitoring is the legality and honesty of revenue collection and expenditure. Moreover, a variety of groups may be watching the performance of local budgets at any given time:

- groups of elected officials (committees, council factions, and so on);
- official auditing agencies, such as national or regional audit or accounting chambers;
- inspectors of individual public services, such as schools;
- NGOs that are primarily concerned with good governance;
- NGOs focused on individual sectors of local public service and concerned about the adequacy and effectiveness of local spending in their specific areas;
- associations of professionals engaged in local government;
- users of local public services;

- competitors of public service organizations, such as alternate producers of those services.

The ability of these observers to evaluate how local budgets are fulfilled depends on their capacity to consider the following aspects:

1. Data presentation and budget classification should be sufficiently detailed. Program budgeting can be used to relate expenditure more clearly to its purpose. Traditional breakdowns by inputs, such as staff salaries, transport, or energy costs, may not show overall expenditure on particular services.
2. Budgeting rules and procedures should be considered. These affect what issues will be discussed, what happens at what stage, who will be involved in the planning, and how they will be involved.
3. There should be good access to fiscal and service performance data. This means public finance should be public, even though town halls may resist demands to show meaningful details of budget allocation or execution, including public contracts.
4. Conflict-of-interest regulations should include codes of ethics that prevent elected officials and civil servants from committing fraud or issuing personal favors.
5. There should be service performance standards and cost comparisons that can be used as a basis for judging efficiency.

6. Reporting should be regular and easily available to elected officials and the general public alike.

To watch in order to intervene

To watch is one thing; to act on observations and secure improvements is another. Two familiar means of intervention are:

- direct participation, principally through voting in elections but also through the use of public hearings and the representation of service users;
- exposure and public pressure, through the media, publication of opinion surveys, performance league tables, and so on.

An alternative approach is the use of incentives through market choice and competition. For example, parents may be able to choose which school their children should attend and the schools might be funded according to the number of pupils they attract. Alternative suppliers of utilities, like telephones or electricity, can be given access to the same distribution system, to allow fair competition.

None of these approaches alone can guarantee effective management of public finance. This is why it is essential to take a range of measures to encourage fiscal transparency as a basic first step in helping ensure proper government spending. ■

The latest issue of "Gosudarstvennoye upravlenie v perekhodnykh ekonomikakh" offers a cycle of articles on fiscal transparency in countries located in this region. This publication is available through ICPS free-of-charge.

To receive your copy, contact Andriy Starynskiy by phone at (380-44) 484-4410 or via e-mail at marketing@icps.kiev.ua.

You can also order the publication on-line at <http://www.icps.kiev.ua/eng/subscribe/>.

Lutsk gets the ISO 9001:2000 Certificate

For three years now, the "People's Voice" project being implemented by ICPS has been instituting best practice in municipal management in the cities and towns participating in this project. Project efforts have always been aimed at encouraging local authorities to provide only high quality services to their communities. After an international conference devoted to the evaluation and standardization of municipal service delivery was held by People's Voice in 2004, the cities of Komsomolsk and Makiyivka received certificates confirming that their systems of service delivery comply with international ISO 9001:2000 standards. Lutsk became the third project city to receive this significant international certificate

Over July–December 2006, the Lutsk City Administration together with the Young Democracy Foundation (Poland) implemented a project called "Through Quality to Transparency." The main purpose of this project was to promote transparency in the work of Lutsk City Hall by introducing the Quality Management System, which complies with the international ISO 9001:2000 standard.

Under the "Through Quality to Transparency" project, a number of innovations were introduced in Lutsk: an Information Point was set up in the City Administration, the place where the first contact between a citizen and city officials generally takes place; information signs and materials were prepared with step-by-step instructions on what a citizen should do in order to solve a problem when applying to the municipality.

All these innovations promote clear and understandable principles of interaction between a resident and the City Administration. Residents receive detailed information on their issues, they know the terms under which an application will be considered and a decision on it made. Thus, any possibility of misunderstanding or abuse of power is eliminated.

In addition, the introduction of the Quality Management System helped to systematize documentation. This had consisted of nearly 100 instructions and description of administrative decision-making procedures, job descriptions, and information cards for the customers, that is, city residents. Finally, a Quality Policy and Quality Book were adopted as the major documents regulating principles and ethics of Lutsk City Administration work.

Also, during the project implementation an electronic system of document flow was introduced in the City Administration. This system enables the total computerization of document processing procedures, both internal and external communication, planning of staff work, monitoring of task implementation, and identification of documents through bar coding.

Having completed the work on documenting the Quality Management System, the Lutsk City Administration conducted an internal audit in order to verify its system, make any necessary adjustments, and take appropriate preventive measures.

The culmination point of the entire project was an external audit of the system by auditors from an independent certification organization called TUV Rheinland

INTERCERT (Poland). Auditors gave the system an excellent grade and their decision was unanimous: they agreed to grant Lutsk City Administration the ISO 9001:2000 International Quality Certificate.

The catch is that an ISO certificate is never granted forever. Every year, independent experts conduct a monitoring audit in order to control the observance of ISO requirements, and every three years a certified organization needs to go through the entire process of certification again. In addition, an organization possessing such a certificate needs to demonstrate to auditors its own improvements to and innovations in the Quality Management System. ■

The International Organization for Standardization (ISO) was set up by delegates from 26 countries in 1947. This is a global federation of national standardization bodies, that is, committees that are ISO members. Its main objective is to help develop globally recognized standards, rules and similar documents with the aim to facilitate international exchange of goods and services in all economic sectors.

The ISO 9001:2000 Standard is an international standard that summarizes advanced global experience in production and service management.

The "People's Voice" project slated for completion in 2007 is being implemented by ICPS, the World Bank and PADCO, a consultancy, with the financial support of the Canadian International Development Agency (CIDA).

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Foreign borrowings on the part of the state are not a threat, for now

During H2'06, the Government turned to foreign lending institutions more often than at any other time in the history of Ukraine: altogether four times. The total amount of loans, US \$1.9bn, is also the largest since 2000. But because these new loans are being signed at the same time as the country pays off its old ones, the country's external debt has only grown by US \$0.5bn over the year. At this point, the increase in national debt does not constitute any threat. The ratio of debt to GDP remains low, only 15.5% at the end of 2006, with 9.5% external debt.

Right now, borrowing externally is better for the country than borrowing domestically, says ICPS economist Oleksandr Zholud. First, it ensures that hard currency comes in to finance the current account deficit that emerged in 2006. In Central European countries, the main source of financing in a similar situation was FDI, but inflows of FDI to Ukraine are insufficient to finance the deficit.

Secondly, when a country borrows on foreign markets, it does not affect private investment domestically. This happens when the state increases borrowing on the domestic market without any increase in the money mass: domestic interest rates tend to go up in this situation, increasing the cost of capital. This leads to less borrowing

in the private sector, that is, business is squeezed out of capital markets by the state. In the end, this means investment in fixed assets goes down and, with it, economic growth.

Although increasing state debt is currently not threatening, Ukraine's overall state and private external debt is growing sharply. ICPS economists estimate that over 2006 it grew more than 24%, reaching 47% of GDP by the end of the year. Private external debt grew the fastest and is already three times higher than public debt. Such rapid growth in debt could lead to problems in the future, especially if the exchange rate begins to fluctuate or the rate-setting policy is changed. Most loans in Ukraine are in US dollars, and this is the currency to which the hryvnia is tied. Should the Government try to devalue the hryvnia as a way to stimulate exports, this would sharply increase the external debt, increasing the risk of a default and making it harder to turn to world capital markets.

Since external borrowings are only one means of financing the Budget deficit, the size of state debt depends directly on the size of this deficit. Thus, according to the ICPS expert, to control the size of external debt, the government should first pay attention to the state of its finances.

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